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MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 2, 2021/2022

BAC3644 –TAXATION 2

(All Sections / Groups)

22 APRIL 2022
9.00 a.m. – 12.00 p.m.
(3 Hours)

INSTRUCTIONS TO STUDENTS

1. This Question paper consists of 12 pages including the cover page with **FIVE (5)** Questions only.
2. Attempt **ALL** questions. The distribution of the marks for each question is given.
3. Please write all your answers in the Answer Booklet provided.

QUESTION 1

Asia Pacific Sdn. Bhd. (APSB) is a tax resident company in Malaysia and has been in the business of manufacturing and assembling of flooring tiles since 2005. APSB also provides interior design service since 2012.

APSB has an issued and paid-up share capital of RM2.12 million and makes up its accounts annually to 30 September. Its statement of comprehensive income for the financial year ended 30 September 2020 is as follows.

| Asia Pacific Sdn Bhd Statement of Comprehensive Income For the year ended 30 September 2020 | | |
|---|-------------|-------------|
| | <u>Note</u> | <u>RM</u> |
| Sales | | 4,450,000 |
| Less: Cost of sales | 1 | (1,370,000) |
| Gross profit | | 3,080,000 |
| Add: Other income | 2 | 866,000 |
| | | 3,946,000 |
| Less: Operating expenses | 3 | (2,145,000) |
| Net profit before taxation | | 1,801,000 |
| Income tax expense | | (432,240) |
| Net profit after tax | | 1,368,760 |

Notes to the accounts:

1. Cost of sales included:
 - i. Provision for stock obsolescence and provision for warranty amounting to RM30,000 and RM25,000 respectively.
 - ii. Compensation of RM14,000 paid to customers due to broken tiles.
2. Other income comprises of:
 - i. Insurance recovery on APSB's product of RM380,000 received from insurance company when the lorry that should have delivered the tiles to a customer in Johor Bahru was involved in accident and caused damage to the product.
 - ii. Interest income of RM222,400 from APSB's investment in a property development project in Malaysia.
 - iii. Gross dividend income of RM200,000 received from APSB's shares in one of a listed company in Bursa Malaysia.

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- iv. The balance was unrealised foreign exchange gains from a purchase of raw materials from Germany.
3. Operating expenses included the following expenses:
- i. Employees' Provident Fund at the rate of 20% from the total remuneration paid by APSB. The total remuneration was RM740,000.
 - ii. Legal fee of RM48,000 for a contract between APSB and a new supplier of raw materials.
 - iii. Legal fee of RM22,500 to defend against a lawsuit brought by a customer who claimed to have suffered an injury due to chipped and cracked tiles installed by APSB's employee.
 - iv. Bad and doubtful debts were in respect of trade debts. They consisted of bad debts written off and a specific provision of bad debts amounting to RM13,400 and RM19,600 respectively.
 - v. Lease rental of RM165,000 for a lorry used to deliver APSB's products to customers. APSB acquired the lorry when it was new in 2019 and paid lease charges totalling RM9,750 in 2019 and RM23,400 in 2020.
 - vi. Training costs of RM10,600 for ten technical employees to attend an approved training for upskilling their knowledge.
 - vii. Advance rental for the company's office which amounted to RM8,600.
 - viii. Cash donation of RM50,000 to UNICEF (an approved institution in Malaysia) as a support to the institution's initiative in providing a better learning environment to poor children.
 - ix. Depreciation of RM101,200 for APSB's assets.
 - x. Interest of RM960 paid for leased lorry [item 3(v)] and interest of RM30,300 paid for the loan used to finance the investment project [item 2(ii)].

Additional information:

For the Year of Assessment (YA) 2020, APSB was entitled to claim an industrial building allowance as well as capital allowance amounting to RM160,000 and RM368,000 respectively. APSB had also disposed its machinery in YA2020 that generated a balancing charge of RM26,400. In addition, APSB had business loss brought forward of RM42,200.

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Required:

Calculate the income tax payable of Asia Pacific Sdn. Bhd. for YA2020.

Note: Indicate 'NIL' in the appropriate column for item that does not require adjustment. Round up all your answers into the nearest Ringgit Malaysia (RM), except for the income tax payable figures.

(20 marks)

QUESTION 2**Part A**

Grand Farm Sdn. Bhd. (GFSB) is a Malaysian tax resident company with accounting year end of 31 December annually. GFSB had been involved in vegetable farming since 2017. In February 2018, GFSB had incurred RM122,000 to replace its harvested cucumber plants with cabbage plants. Later in the year, GFSB had acquired a three-acre land near its current farm to plant corns. Details of expenditure incurred by for its farm are as follows:

| Date | Types of Expenditure | Cost Incurred (RM) |
|------------|---|--------------------|
| 03.01.2017 | Clearing of land for farming | 162,000 |
| 20.02.2017 | Road construction | 78,000 |
| 10.04.2017 | Planting of cucumber seedlings | 210,000 |
| 28.06.2017 | Living accommodation for farm workers | 99,000 |
| 14.12.2017 | Office building and store on the farm | 125,000 |
| 04.02.2018 | Land acquisition for corn plantation | 440,000 |
| 25.05.2018 | Clearing of land for planting corns | 185,000 |
| 08.07.2018 | Planting and fertilising corn seedlings | 97,000 |

On 1 January 2020, GFSB fully discontinued its farming operations after the farm was destroyed by a flash flood. The farm was then sold off for RM900,000 on 11 January 2020 to the land developer.

Required:

- Calculate the agriculture allowance and agriculture charge (if any) of GFSB for the relevant years of assessment. GFSB did not elect for Paragraph 27, Schedule 3 of the Income Tax 1967 (amended). (8 marks)
- Determine whether or not GFSB could claim agriculture allowance on the RM122,000 it incurred to replace the cucumber plants with cabbage plants. Justify your answer. (2 marks)

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Part B

Power Energy Sdn. Bhd. (PESB), which is a Malaysian tax resident company, had bought a power plant for RM980,000 from Paragon Ltd., a company resident in Japan. The purchase transaction took place on 15 April 2020 and the power plant must be installed by Paragon Ltd. For this purpose, Paragon Ltd. sent three of its engineers to Malaysia to install and supervise the operation of the plant from 21 April 2020 to 18 May 2020. PESB paid RM185,000 to Paragon Ltd. for its services on 25 May 2020.

Besides, PESB had also entered into a franchise agreement with Xcellent Ltd., a company resident in India. The term of the agreement required PESB to pay a royalty of RM120,000 to Xcellent Ltd. on 12 December 2020.

Required:

- i. Determine whether or not the above payments made by PESB are subject to withholding tax. Justify your answers.
(4 marks)
- ii. Determine the due date and the amount of withholding tax to be remitted to the Inland Revenue Board of Malaysia (IRBM) for the payment(s) subject to withholding tax.
(3 marks)
- iii. Determine TWO (2) tax consequences for PESB if there is a non-compliance with the withholding tax requirements.
(3 marks)

(Total: 20 marks)

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QUESTION 3

Mr. Toller is a Canadian citizen. He possesses a permanent residence status in Malaysia since the year 2009.

On 6 January 2016, Mr. Toller signed an agreement with Madam Lim for a piece of 5.5-acre land in Mukim Kuala Selangor for RM604,460. Mr. Toller had paid RM45,330 as deposit and would be financing the balance by way of a bank loan. Madam Lim transferred the property to him on 4 April 2016 after receiving the full payment on 25 March 2016. Throughout the acquisition process, Mr. Toller had incurred legal fees of RM7,908 and stamp duty of RM6,302.

In the year 2017, Mr. Toller had spent RM19,450 to level the land. He also incurred another RM11,220 to install a drainage system and fencing around the property. During 2018, Mr. Toller faced a legal challenge over the title of his property from the son of late Madam Lim. Mr. Toller had to engage a lawyer to defend his right, which costed him RM8,340.

In September 2019, his land was inundated by flood due to the high tide phenomenon. He received an insurance compensation of RM13,125 for the resultant damages. Five months later, a landslide damaged Mr. Toller's property due to an improper land reclamation project adjacent to his plot. The project developer decided to settle the matter out-of-court and compensated Mr. Toller RM35,945.

In May 2020, Mr. Toller decided to sell off the land and advertised his intention accordingly. Mr. Melvin Teoh from Sabak Bernam responded and agreed to pay a deposit of RM50,750. However, Mr. Melvin's loan application was unsuccessful and he had to forfeit his deposit. Another prospective buyer, Puan Nurlina had agreed to buy the land from Mr. Toller for RM729,500 in cash. Both Mr. Toller and Puan Nurlina signed the agreement on 15 August 2020 and the payment was made in the same day. The title was then transferred to Puan Nurlina on 1 September 2020.

The entire sales process had costed Mr. Toller RM4,909 for valuation fee, RM1,350 for advertising expense, RM6,001 for real estate agent fee, and RM5,920 for legal fees. Also, up to the time of land sale, Mr. Toller had incurred a total interest charge of RM81,975 on the loan he took upon its acquisition.

Required:

Compute the real property gains tax payable by Mr. Toller upon the disposal of his land.
(20 marks)

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QUESTION 4

Pawsitive Medical Supplies Sdn. Bhd. (PMSSB) was incorporated in the year 2017 with a factory in Ayer Hitam Industrial Park, Johor. It manufactures veterinary medical devices, which are listed by the Malaysian Investment Development Authority (MIDA) as promoted products eligible for tax incentive under the Promotion of Investment Act 1986. It also manufactures pet products and toys for the domestic market, which are not eligible for tax incentive under the same Act.

The finance manager of PMSSB has prepared the following financial details:

| Financial year ended 31 December | Veterinary medical devices manufacturing | | Pet products and toys manufacturing | | Others | |
|----------------------------------|--|------------------------|-------------------------------------|------------------------|--------------------------------|------------------------------|
| | Adjusted income (RM) | Capital allowance (RM) | Adjusted income (RM) | Capital allowance (RM) | Statutory interest income (RM) | Approved cash donations (RM) |
| 2020 | (60,760) | 410,800 | 915,000 | 537,000 | 11,500 | 8,760 |
| 2021 | 970,000 | 447,100 | 947,000 | 612,000 | 9,760 | 12,030 |

The following table presents the qualifying capital expenditures incurred by PMSSB:

| Financial year ended 31 December | Veterinary medical devices manufacturing | Pet products and toys manufacturing |
|----------------------------------|--|-------------------------------------|
| 2020 | RM1,001,100 | RM859,000 |
| 2021 | RM1,024,000 | RM764,000 |

Required:

Compute the chargeable income and amount, if any, to be credited to exempt income for all the relevant years of assessment if:

- i. Pawsitive Medical Supplies Sdn. Bhd. is to apply for pioneer status. (10 marks)

- i. Pawsitive Medical Supplies Sdn. Bhd. is to apply for investment tax allowance. (10 marks)

Note: Provide all relevant workings.

(Total: 20 marks)

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QUESTION 5

You are a certified tax agent and a partner of Messrs. House & Partners, a well-known tax firm in Johor Bahru. You have been assigned to a new walk-in client, Mr. Robert Ho, in 25 February 2021.

Mr. Robert Ho is the owner of a pharmacy in Kluang, Johor. He has received a tax audit notification letter from the Inland Revenue Board of Malaysia (IRBM) dated 21 January 2021. He was requested to produce his relevant documents, records, and receipts along with explanations for his Year of Assessment (YA) 2020 tax filings to the IRBM's Kluang branch. He had waited to consult a tax agent before complying with the request.

Mr. Robert Ho has prepared some information with regard to his pharmacy, as presented in the table below, for your review.

| | 2019 (RM) | | 2020 (RM) | |
|----------------------------|----------------------|----------------|----------------------|----------------|
| Capital | | 111,000 | | 123,000 |
| Profit and loss account | | | | |
| • Balance b/f | 58,000 | | 128,600 | |
| • Add: Profit for the year | 136,000 | | 291,400 | |
| | 194,000 | | 420,000 | |
| • Less: Drawings | (65,400) | | (102,500) | |
| • Balance c/f | | 128,600 | | 317,500 |
| Proprietor's fund | | 239,600 | | 440,500 |
| | | | | |
| Represented by: | | | | |
| Non-current assets | | 133,700 | | 135,300 |
| Current assets | 248,800 | | 454,700 | |
| Current liabilities | (142,900) | | (149,500) | |
| Working capital | | 105,900 | | 305,200 |
| Total net assets | | 239,600 | | 440,500 |
| | | | | |

During your meeting with Mr. Robert, you have also obtained the following information:

- Mr. Robert had acquired RM11,200 in mutual fund units in the year 2015. He had disposed of these in the year 2020 for RM29,500. He then immediately invested the proceeds in shares of energy and healthcare companies listed in Bursa Malaysia.
- He won a cash price of RM12,000 in a Readers' Digest magazine contest in June 2020.
- He bought an apartment in Iskandar Puteri, Nusajaya worth RM536,000. He paid a cash deposit of RM54,000 in October 2019 and financed the balance using a bank loan. The twenty-year monthly instalments of RM4,720 commenced from January 2020.

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- iv. He bought gold jewellery sets for his wife as birthday present in the year 2019 and as anniversary gift in the year 2020. The values of the sets were RM13,300 and RM14,600, respectively.
- v. He sold his Toyota Vellfire for RM195,000 in August 2020. He bought the car in the year 2018 for RM288,000.
- vi. He owned a ten-acre land given to him by his late father who passed away on 6 October 2018. The ten-acre land was valued at RM6,875,000 in the year 2019 and it remained the same in the year 2020.
- vii. Mr. Robert has also listed the following private and personal expenses he estimated to have incurred in the year 2020:

| | RM |
|-------------------------------------|----------------|
| Household expenses | 101,950 |
| Sustenance | 95,250 |
| Medical and life insurance premiums | 16,150 |
| Loan interests | 11,050 |
| Travelling and local vacations | 8,400 |
| Miscellaneous expenses | 7,830 |
| Income tax paid | 2,270 |
| | <u>242,900</u> |

During the meeting, Mr. Robert has confessed that he had discarded all his business records other than cash sales transactions record from the year 2017 onwards. He also did not make appropriate entries for these records in his accounting records.

The meeting ended with you promising to discuss his case with your manager and update him accordingly.

Required:

- i. Based on the information you obtained during the meeting with Mr. Robert Ho, explain to him the non-compliance(s), if any, that he has committed and the consequences.
(8 marks)
- ii. Ascertain whether there is any understatement of income of Mr. Robert Ho for YA2020 by way of capital accretion method.
(12 marks)

(Total: 20 marks)

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APPENDIX**TAX RATES AND ALLOWANCES****i) Tax rates of resident company with paid up capital not more than RM2.5 million**

| Chargeable income | Rate |
|--------------------------|-------------|
| On first RM600,000 | 17% |
| Excess RM600,000 | 24% |

ii) Tax rates of resident company with paid up capital more than RM2.5 million and non-resident company

| | |
|-----------------------|-----|
| All chargeable income | 24% |
|-----------------------|-----|

iii) Non-resident tax rate (other than non-resident company)

| Type of income | Year 2020 |
|---------------------------|------------------------|
| | Rate of Tax (%) |
| Interest | 15 |
| Royalty | 10 |
| Contract payment | 10 + 3 |
| Special classes of income | 10 |
| Public entertainers | 15 |
| Section 4(f) income | 10 |

iv) Capital allowances

| Type of assets | Initial Allowance (%) | Annual Allowance (%) |
|---|------------------------------|-----------------------------|
| Office equipment, furniture and fittings | 20 | 10 |
| Plant and machinery – general | 20 | 14 |
| Plant and machinery (heavy) and motor vehicle | 20 | 20 |
| Industrial building | 10 | 3 |

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v) Agriculture and forest allowance

| | Capital expenditure – Agriculture | Rate of allowance (%) |
|-----|---|------------------------------|
| (a) | Clearing and preparation of land for the purposes of agriculture | 50 |
| (b) | Planting of crops on land cleared for planting | 50 |
| (c) | Construction on a farm of roads or bridges | 50 |
| (d) | Construction on a farm of a building used for the welfare of persons or as living accommodation for a person employed for the working of a farm | 20 |
| (e) | Any other building | 10 |
| | Capital expenditure-Forest | |
| (a) | Construction of roads or buildings used for the purposes of extracting timber from a forest | 10 |
| (b) | Expenditure incurred on buildings used for the welfare of persons or as living accommodation for a person employed in or in connection with the extraction of timber from a forest. | 20 |

vi) Real property gains tax

Disposal by all persons for YA2020

| DISPOSAL PERIODS | PART I Other than Part II and Part III [eg: Malaysian citizen individual, Malaysian permanent resident, partnership, executor of the estate of a deceased person who is a citizen or a permanent resident] | PART II Company incorporated in Malaysia or trustee of a trust | PART III Individual who is not a citizen and not a permanent resident, or an executor of the estate of a deceased person who is not citizen and not a permanent resident, or a company not incorporated in Malaysia. |
|--|--|---|---|
| Disposal within 3 years after the date of acquisition | 30% | 30% | 30% |
| Disposal in the 4th year after the date of acquisition | 20% | 20% | 30% |

Continued...

| | | | |
|--|-----|-----|-----|
| Disposal in the 5th year after the date of acquisition | 15% | 15% | 30% |
| Disposal in the 6th year after the date of acquisition | 5% | 10% | 10% |

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